



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
TEGE EO Examinations Mail Stop 4920 DAL
1100 Commerce St.
Dallas, Texas 75242

501.03-00

Date: February 13, 2012

Number: **201222047**
Release Date: 6/1/2012

LEGEND

ORG - Organization name
XX - Date Address - address

ORG
ADDRESS

Taxpayer Identification Number:
Person to Contact:
Employee Identification Number:
Employee Telephone Number:
(Phone)
(Fax)

CERTIFIED MAIL – RETURN RECEIPT

Dear :

This is a final adverse determination regarding your exempt status under section 501(c)(3) of the Internal Revenue Code. Our favorable determination letter to you dated December 19XX is hereby revoked and you are no longer exempt under section 501(a) of the Code effective January 1, 20XX.

The revocation of your exempt status was made for the following reason(s):

Organizations described in IRC 501(c)(3) and exempt under section 501(a) must be both organized and operated exclusively for exempt purposes. It was determined that you did not meet the requirements for exemption under IRC 501(c)(3). This code section and the related regulations expressly forbid any amount of inurement. Payment of personal expenses on credit cards, payment of telephone bills, payment of automobile payments are example of inurement which occurred.

During the examination it was also determined that you failed to maintain adequate books and records to produce an accurate return as required by IRC 6001 and 6033(a).

Contributions to your organization are no longer deductible under IRC §170 after January 1, 20XX.

You are required to file income tax returns on Form 1120. These returns should be filed with the appropriate Service Center for the tax year ending December 31, 20XX, and for all tax years thereafter in accordance with the instructions of the return.

Processing of income tax returns and assessments of any taxes due will not be delayed should a petition for declaratory judgment be filed under section 7428 of the Internal Revenue Code.

If you decide to contest this determination under the declaratory judgment provisions of section 7428 of the Code, a petition to the United States Tax Court, the United States Claims Court, or the district court of the United States for the District of Columbia must be filed before the 91st Day after the date this determination was mailed to you. Please contact the clerk of the appropriate court for rules regarding filing petitions for declaratory judgments by referring to the enclosed Publication 892. You may write to the United States Tax Court at the following address:

You also have the right to contact the Office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal Appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling. You may call toll-free, 1-877-777-4778, and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at:

If you have any questions, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely,

**Nanette M. Downing
Director, EO Examinations**

Internal Revenue Service

Department of the Treasury
1100 Commerce Street
Dallas, TX 75242

Date: December 21, 2011

ORG
ADDRESS

Taxpayer Identification Number:

Form:

Tax Year(s) Ended:

Person to Contact/ID Number:

Contact Numbers:

Telephone:

Fax:

Certified Mail - Return Receipt Requested

Dear :

We have enclosed a copy of our report of examination explaining why we believe revocation of your exempt status under section 501(c)(3) of the Internal Revenue Code (Code) is necessary.

If you accept our findings, take no further action. We will issue a final revocation letter.

If you do not agree with our proposed revocation, you must submit to us a written request for Appeals Office consideration within 30 days from the date of this letter to protest our decision. Your protest should include a statement of the facts, the applicable law, and arguments in support of your position.

An Appeals officer will review your case. The Appeals office is independent of the Director, EO Examinations. The Appeals Office resolves most disputes informally and promptly. The enclosed Publication 3498, *The Examination Process*, and Publication 892, *Exempt Organizations Appeal Procedures for Unagreed Issues*, explain how to appeal an Internal Revenue Service (IRS) decision. Publication 3498 also includes information on your rights as a taxpayer and the IRS collection process.

You may also request that we refer this matter for technical advice as explained in Publication 892. If we issue a determination letter to you based on technical advice, no further administrative appeal is available to you within the IRS regarding the issue that was the subject of the technical advice.

If we do not hear from you within 30 days from the date of this letter, we will process your case based on the recommendations shown in the report of examination. If you do not protest this proposed determination within 30 days from the date of this letter, the IRS will consider it to be a failure to exhaust your available administrative remedies. Section 7428(b)(2) of the Code provides, in part: "A declaratory judgment or decree under this section shall not be issued in any proceeding unless the Tax Court, the Claims Court, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted its administrative remedies within the Internal Revenue Service." We will then issue a final revocation letter. We will also notify the appropriate state officials of the revocation in accordance with section 6104(c) of the Code.

You have the right to contact the office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling. You may call toll-free 1-877-777-4778 and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at:

If you have any questions, please call the contact person at the telephone number shown in the heading of this letter. If you write, please provide a telephone number and the most convenient time to call if we need to contact you.

Thank you for your cooperation.

Sincerely,

Nanette M. Downing
Director, EO Examinations

Enclosures:
Publication 892
Publication 3498
Report of Examination

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit
Name of Taxpayer ORG		Year/Period Ended December 31, 20XX

LEGEND

ORG - Organization name XX - Date President - president Secretary
- secretary RA-1 - 1st RA CO-1 - 1st COMPANY

Issue:

Whether ORG qualifies for exemption as a public charity under IRC Section 501(c)(3).

Facts:

During the examination of ORG for the year ending December 31, 20XX interviews were conducted with President and Secretary. In addition, credit card statements of President, banks statements of ORG, and the general ledger were examined.

Of concern were issues relating to internal controls, safeguarding assets, inurement and operating in a commercial manner. The books and records could not be reconciled. Income as reported on the books and on the return was off by more than \$ and there was a difference of more than \$ between the expenses as shown on the books and on the return. The organization could not explain the differences.

Secretary indicated that the bank statements were not reconciled monthly.

Of additional concern were purchases on President's personal credit card, payments of telephone bills, payments by the organization on a car loan, and a loan to President in the amount of \$.

An examination of the credit card statements and bank statements found that the organization made \$ of payments on President's personal credit card. This account had four cards issued and these cards were in the possession of various family members. A sample of the credit card statements covering three months of activity (January, March and May, 20XX) found that the vast majority of charges to the account were for items directly related to the operations of the organization. The sample found that % of the charges were for organizational purposes and % of purchases were not be related to the organization. The non-organizational percentage was applied to the total payments of \$ for the year resulting in an estimated \$ of payments on the credit card which had no bearing on the organization. The responsibility to make payments on this credit card was that of President and the organization had no legal liability to make payments.

The examination also found that payments to the mobile phone account of President in the amount of \$ were made by the organization. This account had four separate phone lines. No direct business purpose of this phone account could be determined. While President traveled extensively no need for four lines was determined. Nothing was seen which indicated that phone lines were authorized by the organization.

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Name of Taxpayer ORG		Year/Period Ended December 31, 20XX

In addition to the mobile phones, residential phone service for Secretary and RA-1 was also paid in the amounts of \$ and \$ respectively. This resulted in a total of \$ of payments by the organization on the telephone accounts of President & RA-1 and Secretary.

The organization made \$ of payments on a vehicle during the year which was titled in the names of the organization and President. This vehicle was available to Secretary for unlimited personal use. There was no accountable plan for personal use of the vehicle and no records were seen which document the actual usage of the vehicle. No organizational approval was seen which shows the organization approved the purchase of the vehicle. For purposes of this examination it was determined that President actually owned the vehicle. Payments made on this loan will be treated as compensation.

The examination revealed that a disbursement was made to President in the amount of \$ during a prior year. This disbursement was identified as a loan yet this was not reflected on the return as an asset either as an account receivable or a note receivable. It was established that no note had been signed, no interest was charged, and there was no identified repayment schedule. Ten payments of \$ were made to the organization during the year to repay the loan.

During the initial interview President stated that total fees earned by the organization amounted to \$ per day. Of this, \$ was recognized as income to ORG and \$ was recognized as income of CO-1, President's % for-profit company.

Law:

IRC Section 501(c)(3) states "Corporations, and any community chest, fund or foundation organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, no substantial part of the activities or which is carrying on propaganda, or otherwise attempting, to influence legislation (except as otherwise provided in subsection (h), and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of (or in opposition to) and candidate for public office."

Reg. 1.501(c)(3)-1(d)(1)(ii) maintains that the organization must demonstrate that "it is not organized or operated for the benefit of private interests such as designated individuals, the creator or his family, shareholders of the organization, or persons controlled directly or indirectly by such private interests."

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Name of Taxpayer ORG		Year/Period Ended December 31, 20XX

IRC Section 6001 requires taxpayers to keep and maintain records adequate to determine whether or not an organization is liable for any tax covered by the Internal Revenue Code.

Reg. 1.6001-1(a) says that "Except as provided in paragraph (b) of this section, any person subject to tax under subtitle A of the Code, or any person required to file a return of information with respect to income, shall keep such permanent books of account or records, including inventories, as are sufficient to establish the amount of gross income, deduction, credits, or other matters required to be shown by such person in any return of such tax or information."

IRC Section 6033(a) states in part every organization exempt from taxation under section 501(a) shall file an annual return, stating specifically the items of gross income, receipts, and disbursements, and such other information for the purpose of carrying out the internal revenue laws as the Secretary may by forms or regulations prescribe, and shall keep such records, render under oath such statements, make such other returns, and comply with such rules and regulations as the Secretary may from time to time prescribe..."

Reg. 1.6033-(2)(i)(2) states "Every organization which is exempt from tax, whether or not it is required to file an information return shall submit such additional information as may be required by the Internal Revenue Service for the purpose of inquiring into its exempt status and administering the provisions of subchapter F, chapter 1 of subtitle A of the Code, section 6033 and chapter 42 of subtitle D of the Code."

Rev. Rul. 59-95, 1959-1 C.B. 627 held that failure or inability to file the required information return or otherwise to comply with the provision of section 6033 of the Code and the regulations which implement it, may result in the termination of the exempt status of an organization previously held exempt, on the grounds that the organization has not established that it is observing the conditions required for the continuation of an exempt status.

Discussion:

Evidence found during the examination show that the organization's assets were not being adequately protected and that few internal controls exist within the organization.

The organization's return could not be tied to the books and records and the organization could not explain the differences. The bank accounts were not reconciled on a regular basis.

Four credit cards on the account of President's personal credit card are in possession of four people. A sample of the expenditures shows that personal expenses are being charged to the card and that all payments on the account were made by the organization. It is true that a large majority of the charges were determined to be of a business nature for the organization however more that 12% of the sample covering three months of charges was found to be of a personal nature with no obvious business purpose.

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Name of Taxpayer ORG		Year/Period Ended December 31, 20XX

The telephone payments made by the organization were for residential service for Secretary and RA-1 and for four mobile phones. No business purpose for this was ever established.

The payments on the car loan were for a vehicle which was available for the personal use of Secretary. No records were kept of any personal use. The title of the vehicle was fashioned in the name of the organization and President.

The largest item is a disbursement of \$ which was called a loan but possessed none of the characteristics of a bona fide loan. There was no signed loan agreement or interest charged. In addition there were no scheduled repayments. The disbursement was being repaid at the rate of \$ per month. At that rate it would take more than 200 years to repay the amount of the distribution. It was determined this was not a true loan.

Another significant matter of concern is that the organization was run in a commercial manner. The organization charged a flat rate of \$ per day for services provided. Of this amount the organization recognized revenue of \$ and the remaining \$ was attributed as revenue to President's % for-profit company, CO-1.

In summary the examination found that there is a lack of internal controls and other efforts to protect the organization's assets. No written authorization was seen from the organization or a board of governors for any of the items examined. Charges were routinely made to the personal credit card of President. Personal expenses of several people were paid by the organization during the year under examination. This includes not only credit card charges but payment of telephone bills as well.

The organization operated in a commercial manner when it charged a flat rate for services in the amount of \$ per day for services and then assigned a portion of the income to a for-profit company owned by the president of the organization.

In order to be exempt under IRC Section 501(c)(3) an organization must be organized and operated exclusively for their exempt purpose. Any amount of inurement excludes the organization from exemption. In addition, IRC Section 6033(a) says that an organization must keep and maintain books and records which are adequate to accurately determine the revenues, expenses and financial position of the organization and such information should be accurately reported on returns filed with the Internal Revenue Service.

Taxpayer Position:

The organization's position is not known.

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Conclusion:

During the examination it was determined that the organization did not meet the requirements for exemption under IRC Section 501(c)(3). This code section and the related regulations expressly forbid any amount of inurement. Payment of personal expenses on credit cards, payment of telephone bills, payment of automobile payments and the \$ loan to President are examples of inurement which occurred in this organization. In addition, the organization operated in a commercial manner by charging a flat rate for services. Inurement occurred when a portion of the organization's income was assigned to the for-profit company owned, in part, by President.

During the examination it was also determined that the organization failed to maintain adequate books and records to produce an accurate return as required by IRC Sections 6001 and 6033(a). The balance sheet on the face of the organization's Form 990 did not reflect the loan to President nor did it reflect ownership of an automobile or a related liability for the loan.

It was concluded that this organization does not meet the minimum requirements for exemption under IRC Section 501(c)(3) and its exemption is being revoked effective January 1, 20XX.

Please file US Corporate income tax return Form 1120 for the tax periods ending December 31, 20XX, December 31, 20XX, and December 31, 20XX.

Contributions to your organization are not deductible under IRC 170.